Article

How institutional investors can meet demand for ESG investing

Institutional investors are increasingly interested in environmental, social and governance investments. U.S. Bank experts explain what institutional investors need to consider when implementing an ESG investment strategy.

The trend of environmental, social and governance (or ESG) investing and its outcome-driven cousin, impact investing, has grown rapidly among individual investors in recent years.

More than two-thirds of investors (67%) believe they have a responsibility to invest in companies that make the world a better place, while more than half (51%) say they avoid investing in companies that don't align with their values, according to a survey conducted by MagnifyMoney.

Investment providers have followed suit. More than $51 billion was invested in funds that employ ESG criteria in 2020, which was more than twice as much as the year before, according to Morningstar. In our current social and political environment, interest in impact investing remains high.

Institutional investing and ESG strategy

ESG investing within the institutional realm is increasing, too. About one-third of institutional investors in the U.S. are implementing ESG, according to the Forum for Sustainable and Responsible Investment.[1]

Institutional investors cited a wide range of motivations for implementing ESG criteria, including:

- 57% To align investment strategies with organizational values
- 35% To influence corporate behavior
- 34% To minimize headline risk
- 29% To generate higher risk-adjusted returns over the long term
- 26% To make a better world
- 23% To enhance downside protection
- 17% To benefit from new sources of diversification

Going beyond ESG to DEI

Lisa Isaacson, managing director, strategic initiatives for U.S. Bancorp Asset Management, a wholly-owned subsidiary of U.S. Bank, observed a change in client requests about ESG investing after the summer of 2020.

"Our clients started asking about impact investing more specifically than just environmental, social and governance," she says. "They were interested in investing according to diversity, equity and inclusion [DEI] criteria as well. We saw that 2020 was a flash point for investors to think differently about whether their investments are helping make a better world."

Isaacson lists social equity and social justice as two of the main impact themes that investors are focusing on. "We're also getting more questions from U.S. investors now about carbon and climate change," she says.

According to Breda Sullivan, head of Depositary, Custody and Banking for U.S. Bank Investment Services – Europe, interest in ESG investing among institutional investors is being driven by two main things.

"The first is a desire among these investors to work with asset managers who will invest money in support of their values," she says. "And the second is the regulatory developments in Europe, which give investing in accordance with ESG principals further impetus."

James Byron, vice president of middle office product management at U.S. Bank Wealth Management and Investment Services, says Europe has pushed ahead of the U.S. when it comes to ESG regulation with the Sustainable Finance Disclosure Regulation (SFDR). This imposes comprehensive sustainability disclosure requirements on asset managers and other financial market participants in the EU covering a broad range of ESG metrics.

"One of our European clients needed to comply with Article 8 under the SFDR, and we were able to provide them with the necessary reporting to meet these requirements," says Byron. "In the U.S., institutional clients are asking us for reporting help to demonstrate their ESG ratings on a portfolio level, instead of line-by-line."

Byron notes that from an institutional investor's standpoint, these investors want to work with fund managers who they're confident aren't investing in companies that don't meet their ESG criteria.

"They have choices about which fund managers they use, and ESG compliance is going to play a big role in these choices going forward," he says. "It will help attract more investors who want fund managers to focus on ESG criteria."

ESG best practices for institutional investors

Isaacson urges investors looking to integrate ESG to ask questions about a provider's available strategies and choose one that is supportive of their ultimate investment goals. She also suggests that institutional investors who want to engage in impact investing for a particular outcome should make sure they understand whether data exists to support their objective.

"This space is constantly evolving, and certain disclosures are voluntary, so you need to know whether the impacts you're asking for are supported by the data that's available," she says. "This is a big consideration."

"I recommend focusing on short-term ESG targets that are easily observable and that you can monitor and report on," says Sullivan. "This way, you can make full disclosures and establish credibility that you've set achievable goals. Don't try to boil the ocean."

Byron recommends hiring diverse fund managers (based on their investment strategy) as subadvisors to provide services. "This can help bring diversity of thought to how investment portfolios are run," he says.

Hiring fund managers with different investment strategies can allow service providers, such as U.S. Bank, to take in and report on a wider range of ESG data from their ESG data vendors.

"Also be sure to perform due diligence on the fund manager's approach in relation to investment selection," adds Sullivan.

Our approach to ESG

At U.S. Bank, we address ESG through three pillars that bring together the work across our organization:

1. Lead with core values: Our purpose and core values guide us in everything we do, as does our commitment to doing the right thing for our customers, employees, shareholders and communities. Understanding and managing risk, ensuring proper governance and oversight is in place, supporting the well-being of our employees and ensuring we are meeting our ethical standards are critical to our business.

2. Enable a sustainable future: U.S. Bank set several goals to address our impact on the environment, including a goal to meet Net Zero greenhouse gas emissions by 2050. We support customers and clients in meeting their ESG goals through financing and advisory services. U.S. Bank set an environmental finance goal of $50 billion by 2030, advancing the transition to a low-carbon economy by financing customers and projects that have a positive impact on the environment. Our Commercial Products ESG team guides clients through ESG financing options from ideation to execution.

3. Increase equity, access and economic empowerment: As a bank, we are using our core competencies, such as financial education, home lending, business and consumer banking products, services and experiences to make a difference in the lives of the communities we serve. U.S. Bank Access Commitment, ™ launched in 2021, is our multi-year, multi-dimensional initiative to help close the racial wealth gap. We leverage our work under the Community Reinvestment Act to understand the needs of our communities and deepen relationships in the areas we serve through community engagement and philanthropy.

As ESG continues to evolve we will continue to learn, set ambitious targets, measure our progress and share results.

Whether you're looking for custody, fund servicing, corporate trust, investment management or wealth management solutions, U.S. Bank can help. Learn more about our comprehensive investment services solutions at usbank.com/investmentservices.

[1] www.ussif.org/sribasics